

**ASSEMBLY REPUBLICAN LEADER
DAVE COX**

***GOVERNOR'S
MAY REVISION***

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OVERVIEW

The 2001 May Revision of the Governor's Budget is in stark contrast to the May "Surprise" of the last several years, when extra billions of revenue dollars were thrown on the table by the state's rapidly expanding economy. This year, the May Revision heralds a sinking economy, driven by dot.com failures and energy woes, which at face value should lead to a reexamination of the state's budget priorities and a reconfiguring of its spending totals to match expected revenues. The Governor's May Revision, however, attempts to paper over the significant decline in the state's fiscal fortune through a series of sleight-of-hand gimmicks – fund transfers, fund shifts, redirections and spending of reserve funds – that are reminiscent of the early 1990s. While the Governor has withdrawn some of the new program proposals he made in January, he has completely ignored the opportunity to weed out lower priority and failing programs, and thereby improve the state's ability to weather worsening times. Along with a measly reserve fund of only \$1 billion, these actions raise the question of how the state will respond if revenue collections continue to be weak.

The Department of Finance suggests that they faced a \$5.7 billion "problem" in preparing the May Revision, as shown in Table 1. As the table shows, this \$5.7 billion problem consists of the net 2-year reduction in General Fund revenues of \$4.2 billion and a \$1.5 billion increase in spending requirements. Table 1 also details the Governor's overall approach to resolving the problem, which consists mostly of using reserves and transfers to make up for the lost revenue and increased spending. Of the \$2.5 billion labeled as "Funding Shifts and Program Reductions, our preliminary estimates indicate that no more than \$1 billion represents program reductions, and most of those represent reductions in new programs or program expansions proposed in January. The Department of Finance was unable to provide any details on specific program reductions as of this writing.

Table 1
The 2001 May Revision Budget Problem
(\$ in billions)

Problem:

Reduction in General Fund revenues:	\$4.2
Increased Proposition 98 requirements	0.6
Increased caseload and other required costs	<u>0.9</u>
Total, budget problem	\$5.7

Solutions:

Reduced Reserve Funds	\$1.3
Transfer of Transportation Sales Tax	1.3
Transfer of Other Special Funds	.6
Funding Shifts and Program Reductions	<u>2.5</u>
Total, budget "solution"	\$5.7

As the Department of Finance's figures show, the Governor's strategy has been largely to finagle ways to maintain existing spending levels rather than develop a sustainable spending plan with adequate reserves. Assembly Republicans believe that, with appropriate reductions in spending, this year's budget could provide full funding for K-12 education and public safety, a 4 percent reserve fund and the elimination of the ¼ cent sales tax increase assumed by the Governor. Such a strategy would enhance the state's flexibility to deal with increasingly uncertain times.

REVENUES AND EXPENDITURES

- ◆ **California Economy Growing but Slower.** While the nation's economy has clearly slowed, the state's has shown continued momentum. As past declines have demonstrated, however, California is able to *outperform* the national economy, but it is not able to *outlast* it. The May Revision assumes that the national slowdown will begin to be felt in California in the months ahead, with job growth falling to 2.3% in 2001, compared to 3.8% in 2000. No mention is made in the May Revision of the potential impacts of the energy crisis on the state's economy, however, a pick-up in the economy is expected in 2002.
- ◆ **Stock Market Bubble Bursts.** Of major portent for state revenue collections, the May Revision documents a huge decline in state personal income attributable to the decline of the technology sector. Stock options have made up a large and increasing share of personal income in recent years, so the collapse of the bubble is expected to have a huge impact. The May Revision assumes that stock option income declines by 37 percent, back to about 1999 levels. Capital Gains realizations are now expected to decline 27 percent, compared to the 10 percent decline expected in January.
- ◆ **General Fund Revenues Up and Down.** Current year revenues are estimated to exceed the January budget forecast by over \$1.1 billion, reflecting strong stock option and capital gains activity in 2000. Revenues for the 2001-02 fiscal year, however, are forecast to decline by almost \$4.6 billion, or by about 6 percent.
- ◆ **General Fund Spending Slightly Affected.** The May Revision indicates that General Fund spending proposed for 2001-02 is expected to be \$79.7 billion, which is about \$2.2 billion less than proposed in January. However, the \$2.2 billion figure overstates the amount of spending reductions actually proposed in the May Revision, because of the extensive use of redirections and funding transfers. As noted earlier, our preliminary estimates indicate that actual spending has been reduced by no more than \$1 billion.
- ◆ **Governor's January Proposals Withdrawn.** Much of the reduction in spending that is present in the May Revision reflects the Governor's decisions not to proceed with spending initiatives he championed in January. Few of the reductions affect programs established in prior years and now considered to be part of the state's spending "base."
- ◆ **Fund Transfers Take Advantage of Idle Funds.** The Governor's advisors have informed us that the proposed fund transfers generally take advantage of situations where funds are underutilized or are temporarily unavailable. The largest of these is the transfer of transportation sales tax revenues, where delays in project delivery have led to an accumulation of revenues.

The remainder of this document reviews the major May Revision proposals by subject area and provides some indication of our initial reactions to these proposals.

HEALTH AND HUMAN SERVICES

In contrast to the lower spending totals in other parts of the May Revision, total General Fund expenditures proposed for Health and Human Services are now \$21.9 billion, which is an increase of \$200 million above that proposed in January. The net increase is generally attributable to increases and offsetting decreases in various caseload driven programs, and the need to reduce funding in order to manage state programs within available General Fund resources.

- ◆ **Healthy Families Program (+\$10 million GF).** While the budget proposes increased General Fund expenditures of \$10 million, net expenditures are expected to decrease by \$76.9 million (\$44 million Tobacco Settlement Fund) below the level proposed in January. This net expenditure decrease is primarily due to the postponement of the Healthy Families Parent Expansion until October 1, 2001, as a result of a delay in obtaining the approval of the waiver from HCFA. The program is expected to serve 525,000 children and 158,000 adults by June 30, 2002, which represents a decrease of 36,000 children and 16,000 adults compared to the Governor's Budget.
- ◆ **Medi-Cal Program (+\$367.7 million GF).** The Medi-Cal caseload is expected to increase by 233,400 to 6,084,200 eligible beneficiaries (4 percent over the January budget). General Fund increases include \$255.1 million for the Orthopaedic Hospital Outpatient settlement; \$46.1 million for a long term care rate increase (2.15 percent for nursing homes), and \$25 million for a managed care rate increase (2 percent).
- ◆ **Reduction in Public Health Caseload Programs (-\$3.9 million GF).** The Administration has proposed a decrease of \$3.9 million due to decreased health care costs in the California Children's Services, Child Health and Disability Prevention, and Genetically Handicapped Persons programs.
- ◆ **County Outreach for Medi-Cal and Healthy Families Programs (+\$22 million FF).** An increase of \$22 million of Federal Title XXI administrative funding is proposed to fund County Outreach programs for the Medi-Cal and Healthy Families Programs.
- ◆ **Grants to Local Public Health Departments (-\$2 million GF).** The May Revision proposes to eliminate a \$2 million augmentation for local public health department subventions.
- ◆ **Prospective Reimbursement for Federally Qualified Health Centers and Rural Health Clinics (\$2.6 million GF)** – The Governor proposes an increase of \$2.6 million to implement a new prospective payment system for Federally Qualified Health Centers and Rural Health Clinics as federally required by the Beneficiary Improvement and Protection Act.
- ◆ **Regional Center Backfill due to Reduced Federal Participation (+\$8.8 million GF).** The Administration proposes to replace reduced federal funds on a dollar for dollar basis. Delays in recertifying California's Regional Center Medicaid Home and Community - Based Waiver resulted in a loss of federal funds totaling \$5.6 million. Additionally, billings for Targeted Case Management billings and base rates for Regional Center administrative costs failed to rise to anticipated levels resulting in a corresponding need to replace reduced federal revenues with \$3.2 million GF.
- ◆ **Regional Center Caseload (+\$32.9 million GF).** The Regional Center caseload is growing faster than anticipated by the proposed Governor's Budget. Based on new projections, the Budget Year caseload will exceed that projected in the Governor's proposed Budget by 1,075 clients or .6 percent. Because of this increase the Administration is proposing an increase of \$33.4 million (\$32.9 million GF) to fund the additional staff to care for these individuals and purchase the services to which they are entitled.

- ◆ **Early Start Program (-\$2.6 million GF).** Declining revenues forced the Administration to abandon its proposed increase of \$2.6 million GF which would have been used to expand resources to more fully evaluate children for eligibility and necessary services. As proposed this augmentation would have ensured compliance with federal and state requirements to conduct multidisciplinary evaluations and assessments within 45 days of a child being referred to a Regional Center.
- ◆ **Mental Health (-\$16.6 million GF).** The Administration's May Revision proposes reducing the Budget Year allocation by a net of \$16.6 million GF. This adjustment is comprised of the following: 1) an increase of \$2.4 million GF to pay the higher cost of new psychotherapeutic drugs in State Hospitals; 2) an increase of \$2.6 million (\$2.1 million GF) for recruitment and retention bonuses for classifications that have been difficult to recruit i.e., psychiatric social workers, and psychologists; 3) a reduction of \$12.4 million for deferred maintenance projects; 4) deletion of the planned \$5.0 million or 3% discretionary COLA for mental health managed care programs; and 5) a reduction of \$5.0 million proposed to expand the supportive housing program.
- ◆ **Department of Alcohol and Drug Programs (- \$45.1 million GF).** The Administration proposes to reduce Current Year expenditures by \$21.5 million (\$10.4 million GF) because of a significant delay in securing appropriate State Medicaid Plan amendments that would have, effective January 2001, permitted new Drug Medi-Cal services. Budget Year proposals reflect a reduction of \$34.7 million. This reduction is primarily composed of the following: 1) an increase of \$22.4 million (\$10.9 million GF) to serve a Drug Medicaid caseload increase of 20,700 new cases; 2) reductions totaling approximately \$72 million (\$46 million GF) comprised of: a) \$7.7 million for expansion of adult treatment services; b) \$5.7 million for expansion of youth treatment services; c) \$50 million (\$24.3 million GF) reflecting a federal delay in approving a State Plan amendment authorizing federal funding for the discretionary expansion of Drug Medi-Cal day care services; and c) a reduction of \$8.5 million GF for Drug Court substance abuse treatment.
- ◆ **Department of Social Services (-\$96.2 million GF).** The Administration proposes to reduce General Fund expenditures in the CY by \$50.9 million and in the BY by \$45.3 million to reflect caseload reductions. IHSS expenditures reflect augmentations in the BY totaling \$57 million GF to further specific goals of the Administration's Aging with Dignity initiative, improve the quality of provider services and strengthen provider staff recruitment and retention.
- ◆ **Department of Aging (-\$2.5 million GF).** The Administration's May Revise proposal reflects a BY reduction of approximately \$2.5 million GF. This reduction includes the elimination of the previously proposed augmentations of \$1.5 million to expand the Linkages program and an approximately \$1.0 million for Adult Day Health Care.

EDUCATION

In January, the Governor proposed to fund Proposition 98 at the “Test 2” level, which required total state and local funding of about \$46.0 billion, including state General Fund appropriations of \$32.5 billion. In the May Revision, the Governor has sacrificed this goal of meeting the “Test 2” funding level. Instead, he has reduced the level of total Proposition 98 funding for 2001-02 by \$383 million, leaving the 2001-02 funding \$861.1 million short of the Test 2 funding level. However, the May Revision also recognizes a prior-year settle-up obligation of \$540.8 million. Including these funds, the May Revision provides about \$158 million more for 2001-02 than did the January budget. The \$861.1 million “shortfall” will be paid as a “maintenance factor” in the 2002-03 fiscal year.

Including the settle-up funding, per-pupil spending is \$7,168 compared to \$7,174 in January. The May Revision includes nearly \$150 million to provide for an increase in the statutory growth rate from 1.06 percent to 1.40 percent. The May Revision also accounts for a decrease in the COLA from 3.91 percent to 3.87 percent.

K-12 EDUCATION

- ◆ ***Middle Grades Extended Year (-\$35 million).*** The Governor revised his proposal to extend the middle school year from an additional 30 days to 20 days, and redirected the cost savings to support low-performing schools. The budget year appropriation has been reduced from \$100 million to \$65 million, with \$300 million proposed in 2002-03 and \$650 million in 2003-04 to fully fund three middle school grades.
- ◆ ***New Block Grant Programs (+\$220 million).*** The May Revision proposes two new block grant programs targeted toward the lowest performing schools. These include: (1) \$220 million for the High Priority Students Block Grant Program to provide schools in the lowest two deciles of the Academic Performance Index (API) with \$175 per pupil for three years; and (2) the Targeted Instructional Improvement Block Grant, which consolidates existing funding (nearly 1.2 billion) for the Court-Ordered and Voluntary Desegregation and the Economic Impact Aid Programs.
- ◆ ***Mathematics and Reading Professional Development Program (-\$175 million).*** The May Revision reflects a reduction from \$335 million proposed in January to \$160 million, which accounts for teachers who have received or will receive training through the Professional Development Institutes operated by the University of California. The program will provide standards-based training to 217,000 K-12 teachers and 22,000 instructional aides over a period of three years.
- ◆ ***School Energy Cost Assistance (+\$540.8 million).*** The May Revision provides \$540.8 million in Proposition 98 settle-up funds to provide assistance to school districts to pay for increased energy costs and to improve energy efficiency. School districts will be required to commit to conservation measures that will lead to a 10 percent reduction in energy use.
- ◆ ***School Readiness (+\$3 million).*** The May Revision provides \$3 million for the development and validation of assessment instruments to determine children’s readiness to learn prior to entering school.
- ◆ ***Immediate Intervention/Underperforming Schools Program (II/USP)(+\$49 million).*** The May Revision provides full funding for implementation grants at \$200 per pupil for the current year and budget year. State funding for the current year is \$168 per pupil, while federal funding provides \$200 per pupil.

- ◆ **Governor's Performance Awards (-\$123 million).** The Governor proposes to eliminate the \$123 million augmentation for the Governor's Performance Awards program, which would have fully funded the program at \$150 per test taker. The awards are currently funded at \$68 per ADA. Republicans have supported full funding for the awards to provide incentives to low performing schools.
- ◆ **Adjustments in Program Participation (-\$172 million).** The May Revision reflects a number of reductions based on participation in programs, such as the Instructional Time and Staff Development Reform Program (\$35 million reduction), the new Algebra Incentive Program (\$10 million reduction), and 9th grade Class Size Reduction in two courses (\$30 million reduction), among others.
- ◆ **After School Programs (-\$20 million).** The May Revision eliminates the \$20 million half-year expansion for the Afterschool Learning and Safe Neighborhoods Partnerships program.
- ◆ **Deferred Maintenance (-\$8.8 million).** The May Revision proposes to reduce funding for the Deferred Maintenance Program to the funding level provided in the current year.
- ◆ **Child Care (+\$131.5 million).** The May Revision provides an increase of \$131.5 million from primarily federal sources to fully fund CALWORKS Stage 2 childcare. The Governor did not provide additional funding for childcare services for families transitioning off of welfare. The Governor's proposed budget fully funded services for these families through only July 2001. The administration is in the process of finalizing its review of child care policies and resources to address equity in access to child care services for these families and the working poor.

HIGHER EDUCATION

- ◆ **Community Colleges (+\$37 million).** The May Revision reflects an increase of \$37 million General Fund for local assistance and \$53,000 General Fund for state operations.

The May Revision reflects the following increases:

- \$49 million in one-time funds from the Proposition 98 Reversion Account to assist colleges with a portion of their natural gas and electricity costs and to promote conservation efforts.
- \$13 million as a result of changes in local revenue, revised COLA, and other baseline adjustments.
- \$407,000 for the Chancellor's Office to obtain space within its headquarters building.

The proposed increases are partially offset by the following reductions in augmentations proposed in January:

- \$5 million for the Teacher and Reading Development Program.
 - \$10 million for Scheduled Maintenance.
 - \$10 million for Instructional Equipment and Library Materials.
 - \$460,000 for state operations.
- ◆ **University of California (-\$16.7 million).** The May Revision reflects a reduction in the university's General Fund augmentation from \$202.5 million proposed in January to \$185.8 million.

The May Revision reflects the following increases:

- \$100.6 million for increases in natural gas costs and to promote energy conservation.
- \$12.8 million for a projected increase in enrollment of 1,400 FTE students.

The May Revision proposes the following reductions from the January budget:

- \$89.8 million to reduce Partnership funding from four to two percent, and to eliminate the one percent funding to address budget shortfalls in ongoing building maintenance, instructional equipment, instructional technology and libraries.
- Eliminate \$20 million in one-time funding for instructional equipment, deferred maintenance, and instructional materials.
- Eliminate \$5 million in one-time funding for research in engineering and computer science.
- Eliminate \$5 million in one-time funding for research in environmental science.
- Reduce funding by \$5 million for the Professional Development Institutes.
- Eliminate \$1.5 million expansion for graduate and professional school outreach.

The May Revision also proposes to shift \$188.6 million in capital outlay projects, including UC Merced, from one-time General Fund support to Lease Revenue Bond Funds.

- ◆ **California State University (-\$58.8 million).** The May Revision reflects a reduction in the university's General Fund augmentation from \$216 million proposed in January to \$157.2 million.

The May Revision reflects an increase of \$34.1 million for increases in natural gas costs and to promote energy conservation.

The May Revision proposes the following reductions from the January budget:

- \$70.2 million to reduce partnership funding from four to two percent, and to eliminate the one percent funding to address budget shortfalls in ongoing building maintenance, instructional equipment, instructional technology, and libraries.
 - Eliminate \$20 million in one-time funding for instructional equipment, deferred maintenance and instructional materials.
 - Eliminate a \$1 million augmentation for CSU's Program for Education and Research in Biotechnology.
 - Eliminate a \$1 million augmentation for the Diagnostic Writing Service.
- ◆ **Student Aid Commission (-\$35 million).** The May Revision reflects a reduction of \$35 million for Cal Grants for both the current and budget years (\$70 million total). The number of eligible applicants for the Cal Grant Entitlement awards is estimated to be less than that projected in the January budget. In addition, factors such as more students selecting lower cost public institutions contributed to savings in the current year.

RESOURCES AND ENVIRONMENTAL PROTECTION

Resources and environmental protection funding was affected very little by the May Revision. Most of the Governor's January proposals remain intact and there are even some small augmentations for emerging issues that need to be dealt with in the budget year. The biggest surprise was the decision to fully fund the state's share of CALFED after the federal government reduced their expected contribution of \$400 million to only \$20 million. Flood control subventions, clean beaches, and river parkways all experienced significant reductions from the January proposals. Other programs of less or questionable value were not reduced.

- ◆ ***Stringfellow/Casmalia Hazardous Waste Sites Settlement (+114.5 million)***. The May Revision proposes \$114.5 million to settle the state's liability at these decades-old Superfund sites. In a negotiated settlement with the federal government, the state will be allowed to buy out for less than the estimated cost of clean-up, of up to \$183 million.
- ◆ ***Hexavalent Chromium Studies – (+\$462,000)***. Due solely to the success of the movie “*Erin Brockovitch*”, which was based on questionable science, the Governor is allocating funds to collect data on water systems throughout the state and to begin cleanup activities on those wells determined to be contaminated.
- ◆ ***Drought Panel Recommendation Funding- (+10.5 million)***. In addition to funding specific projects, the Governor has allocated an unspecified amount to address emergency drought conditions in the Klamath Basin. The drought funding package includes \$1 million for the EIR for a critical water shortage purchasing program, \$1.5 million for technical assistance to rural homeowners and small water systems on private wells, \$6 million for technical and financial assistance for local agencies to collect data and develop groundwater management plans, and \$2 million for technical and financial assistance for local agencies to develop integrated water resource management plans. The May Revision is very short on details for this new initiative.
- ◆ ***Water and Energy Efficiency Program- (+\$5 million)***. This is another technical assistance and funding program with little detail. This program will encourage efficient water and energy use in urban and agricultural areas. The only information provided is that this program will save 630,000 acre feet of water and 38 MW of power.
- ◆ ***California Oak Mortality Recovery Program (+1.9 million)***. This represents much less than current legislative proposals for \$5 to \$10 million. Instead, the Governor's May Revision proposes funding of \$1.9 million for additional studies on Sudden Oak Death Syndrome and for hazardous tree removal.
- ◆ ***Electrical Generation Plant Inspections (+5.5 million)***. This is a set-aside to be used when clarification of the oversight and enforcement functions of a State power authority, the Public Utilities Commission, the Independent System Operator and the Electricity Oversight Board are established. These funds are to be used for development and enforcement of generation plant performance standards, including maintenance schedules and programs. The funds are supposed to ensure that generators don't shut down for unscheduled maintenance during shortages to drive up prices.
- ◆ ***Foreign Animal Disease (+\$1.4 million)***. This funding is proposed for planning, media relations, outreach, and education for a foreign animal disease preparedness program. Presumably, this money will be used by the Department of Food and Agriculture in the event that mad cow disease or hoof and mouth disease are discovered among California livestock or in foreign meat products imported into the state.

- ◆ **Clean Beaches Initiative (-\$90 million).** The \$100 million proposed in the January budget has been reduced to \$10 million. There were no specifics contained with the recommendation as to revised spending criteria.
- ◆ **Brownfields Insurance Program (-\$37.5 million).** The program budget proposed in the Governor's Budget has been eliminated. In January, the budget provided \$40 million for this program. There is no explanation for the \$2.5 million discrepancy between January and May.
- ◆ **River Parkway Program (-\$35 million).** One half of the January budget proposal of \$70 million has been deleted from the budget. The remaining \$35 million is allocated for specified carve-outs, including \$5 million for the Cornfields property at Chinatown in Los Angeles. This amount is to be supplemented with \$35 million in Proposition 12 funds. \$6 million is allocated for the acquisition of Wrigley Heights in the City of Long Beach. Many people will be surprised to learn that the LA River goes to Long Beach instead of through the outlet channel at Marina Del Rey. \$4 million is for the acquisition of Spano Ranch in Fresno and Madera counties. \$8 million is for unspecified acquisitions in Stanislaus County. \$1 million is for trail development in the City of San Jose and \$1 million for Fenwood Ranch on the Sacramento River in Shasta County.
- ◆ **Flood Control Subventions (-\$50 million).** Although nowhere to be found in the May Revision document, the Department of Finance briefing indicates that the January proposal for \$74 million to fund all due-bills for flood control projects has been reduced by \$50 million. The balance of \$24 million is reportedly sufficient to pay current claims.
- ◆ **Ongoing State Park Maintenance (-\$9 million).** The May Revision reduces the \$11 million allocation proposed in January for inspection and regular maintenance on State Park facilities. This proposal was supposed to prevent significant future costs in deferred maintenance.
- ◆ **Diesel Emissions Reductions for Peaker Plant Offsets (-\$68 million).** \$32 million remains from the \$100 million January budget proposal. This program is to provide funds to replace diesel engines on trucks and machinery in order to reduce NOX emissions and create air credits to offset the impacts of peaker plant operations.
- ◆ **Zero Emission Vehicles (-\$50 million GF).** Not a reduction, but a fund shift of \$50 million from the General Fund to the Motor Vehicle Account. In January, the Governor proposed \$50 million to provide grants of \$5,000 per vehicle to encourage the purchase of 9,000 to 10,000 electric cars. He also proposed grants to defray the costs of home wiring and charger installations. The program is still in effect with a different funding source.

TRANSPORTATION

There are few new transportation spending initiatives in the May Revision. The story in this area is the Governor's proposal to reverse last year's major decision requiring that revenues from the sales tax on gasoline be dedicated to transportation projects. The Governor proposes several other fund shifts and borrowing mechanisms, again with the goal of replacing lost General Fund revenues in order to maintain spending. The Governor maintains that this financial shell game will not result in any losses to the programs approved last year in the Traffic Congestion Relief Plan.

- ◆ **Refinancing the Transportation Funding Plan(+ \$1.3 billion).** The May Revision defers the transfer of the sales tax on gasoline for two years to create a General Fund "savings" of \$1.3 billion in 2001-02 and \$1.2 billion in 2002-03. The rationale for this transfer is that more money is coming in to the Plan's fund than can be spent on projects in the next few years. The

Governor proposes to defer the sales tax shift for two years and keep the plan whole by adding two years after the statutory termination date of 2005-06. With this change, the program will extend out to 2006-07 and 2007-08. By adding two years to the program, the Administration asserts that there will be an additional \$500 million available for funding the projects, but this obviously ignores the impact of inflation on the costs of projects that will be delayed. The Governor states that no projects will be delayed by the shift, which we interpret as an admission by the Governor that no projects were going to be delivered for the next few years. Interestingly, although the cost of gasoline has nearly doubled in 2001, gasoline sales tax revenues are down slightly from the January projections. There is no explanation offered for this.

- ◆ **Local Streets and Roads Maintenance Funds Backfilled.** The May Revision proposes to backfill the existing local streets and roads and road maintenance programs funded by gasoline sales tax dollars with State Highway Account dollars for two years. After that time, assuming that the General Fund is healthy again, the program will resume funding with the sales tax revenues. The Governor explains that this can be viewed as a “refinancing” plan to provide cash for the General Fund without jeopardizing the projects and programs negotiated last year. Again, we interpret this as an admission that SHA project delivery will continue to lag promised levels.
- ◆ **Installation of Battery Back-ups and energy Efficient Lighting Devices at Intersections (+\$21.4 million).** These funds will be utilized to ensure the operation of traffic signals in the event of a power outage.
- ◆ **Increased Federal Funding For Farmworker Transportation (+\$500,000).** Provides additional spending authority for federal grant funds to purchase and operate vans and buses to transport farm workers to the fields.
- ◆ **E-Government License Plate Initiative- (+\$592,000).** Funds are allocated from the Motor Vehicle Account to develop software to allow the public to use the Internet to order and buy personalized license plates. This certainly should qualify as a top priority in a fiscally constrained year.
- ◆ **E-Government Customer Services- (+\$2.7 million).** The May Revision provides funds for DMV to develop a Spanish website, purchase advance speech processing software to improve telephone service to the public, and test an automated e-mail response system.
- ◆ **Queuing System Expansion- (+\$2.5 million).** Funding proposal to manage the lines that form in 66 DMV field offices and 8 regional offices. According to the May Revision there is a system that can be purchased to make lines move faster.
- ◆ **VLF Reduced Administrative Costs- (-\$3.4 million).** A budget reduction of \$3.4 million and 68 personnel years is proposed. Instead of issuing individual checks in the new budget year, the Governor proposes to significantly reduce the cost to administer the program by applying the discount directly to the license renewal form. Why didn't we think of that?
- ◆ **Reducing the Excess Balance of the Smog Impact Fee Refund Account-(Fund Transfer of \$96.4 million to the General Fund).** The May Revision transfers \$96.4 million from the smog refund account back to the General Fund. New estimates of the resources needed indicate that the reduction would not affect any refunds due. The number of actual applications for refunds has not been at the volume initially anticipated based on the registrations that could qualify for a refund.

GENERAL GOVERNMENT

- ◆ Across The Board Reduction (-\$50 million). The May Revision proposes a new control section reducing all state operations budgets by 2.5 percent, with exclusions for fire/life safety, 24 hour care and revenues producing agencies. Our estimates suggest such a reduction should actually produce several hundred million dollars in savings.
- ◆ **Electrical Generation Plant Inspections (+\$5.5million).** The May Revision contains a new spending proposal for \$5.5 million for electrical generation plant inspections. There have been some allegations that these plants are operated in a way that adversely impacts the supply of power on the grid. The location of the funding is unspecified. Funding will be made available upon clarification of the oversight and enforcement responsibilities of the PUC, ISO and EOB.
- ◆ **Low-Income Housing Programs (no reduction).** The May Revision retains the funding levels for most of the housing funding proposals from last year totaling approximately \$314 million. This funding is used for existing low-income housing programs that provide subsidized housing and do not address the fundamental problem of increasing the supply of housing.
- ◆ **Jobs Housing Balance Program (-\$200 million).** The Governor does eliminate \$222 million in proposed funding for housing programs. A \$200 million reduction is from the Jobs-Housing Balance/local permit program that provides grants to those local governments that establish an increase in building permits issued. This program received \$100 million in initial funding in the 2000 Budget Act and because that money went unused, the program would have contained a total of \$300 million in an unproven program. Republicans would like to see an elimination of the \$100 million in current year funding. Assembly Republicans believe these funds would be better used to increase discretionary funding for local governments.
- ◆ **School Facilities Fee Assistance (-\$126 million).** The Governor also eliminated the future appropriations related to the School Facilities Fee Assistance Program (\$40 million in 01-02 and \$20 million in 02-03) and transferred the uncommitted remaining balances in the existing funds (approximately \$86 million) to the General Fund. These programs were linked the passage of Proposition 1A and to prospective homebuyers and locally charged school facilities fees. These programs have been an abysmal failure.
- ◆ **Homebuyers Downpayment Assistance Program (-\$18 million).** The Governor is transferring \$18 million of the \$50 million in current-year funding to the General Fund from the California Homebuyers Downpayment Assistance Program. It is unclear why this funding is being transferred, since the program is very popular and does not lack from qualified participants.
- ◆ **Infrastructure Bank (-\$177 million).** The May Revision contains a transfer of \$177 million from the California Infrastructure Bank, leaving a balance of approximately \$325 million. The Technology, Trade, and Commerce Agency has done a poor job in getting the money out the door, which is why the Bank has such a large balance. The May Revision also eliminated most of the new funding proposed for several programs under the Technology, Trade, and Commerce Agency, totaling over \$8 million.
- ◆ **Cultural Infrastructure Development Fund (-\$14 million).** This fund is under the California Arts Council and its purpose is to fund local infrastructure art programs. The May Revision reduces the proposed funding from over \$20 million in 2001-02 to \$6 million. Significant funding for local art programs makes no sense when local governments do not have enough money to fund homeless shelters or police officers.
- ◆ **California Veteran Homes (+5 million).** The May Revision contains over \$5 million for two veteran homes. Over \$2 million is proposed for the Yountville Home for business process re-

engineering and \$2.8 million to the Barstow Home due to its de-certification and the loss of federal funding.

- ◆ ***Touch Screen Voting Pilot Program (-\$48 million).*** The May Revision deleted the proposed \$40 million for a touch screen voting pilot program in three unspecified counties. Assembly Republicans believed that a touch screen voting pilot project is unnecessary because Riverside County has already done a pilot program, and in fact, has implemented a touch screen voting system during the last election. The County has received a 98% acceptance rate from the voters. In addition, during the last election, there were 6 counties that implemented a pilot a touch screen program, including San Diego and Alameda.
- ◆ ***Department of Industrial Relations (-\$2.4 million).*** The May Revision contains reductions of \$2.4 million in new spending for workers' safety and labor law compliance efforts. Assembly Republicans would like to see further reductions of over \$3 million from this department in its labor standards enforcement division due to the department's very high vacancy rate.
- ◆ ***Higher State Agency Utility Costs (+\$39.2 million).*** The May Revision proposes additional funding for state agency energy cost increases. The Governor's January 10, 2001 budget proposed \$50 million (\$25 million General Fund) for current year costs. The May Revision proposes an additional \$39.2 million to address higher utilities costs in 2001-02.
- ◆ ***State Tax Collections (+\$7.6 million).*** In an effort to increase the state's revenue, the May Revision contains \$7.6 million for 123 new positions at the Franchise Tax Board. It is assumed that the new positions would be for additional tax auditors and collectors. The Governor is estimating that this proposal would generate revenues of \$53.8 million in 2001-02 and \$97.5 in 2002-03. If the Governor really wanted to generate more revenue from taxpayers, he should look at FTB's \$3.2 billion in uncollected revenue involved in "protest" cases. Some of these cases are over 5 years old. The Governor should consider resolving these cases from the current 48 to 33 months to 24 months. Resolution of these cases would result in approximately \$500 million to the General Fund in 2001-02.

TAX RELIEF

Targeted Tax Relief (-\$38 million)

The May Revision reflects a decrease of \$38 million for targeted tax relief from the Governor's January 10, 2001 Budget proposal. The Governor's January 10, 2001 Budget proposed only \$108 million in targeted tax relief for 2001-02, and more importantly, did not retain the ¼ cent sales tax reduction that became effective on January 1, 2001. The Governor's action will effectively raise taxes by \$1.2 billion annually when the ¼ cent sales tax is reestablished in 2002. Once again, the Governor choose not to provide important, and timely, tax relief to working families and California's businesses, who will also see substantial increases in their energy bills when the Governor's rate increases take effect this summer. The May Revision continues only the following targeted tax relief proposals:

- ◆ *(Increases the Manufacture's Investment Credit).* Increases the credit from 6% to 7%. This is a step in the right direction. Assembly and Senate Republicans proposed to increase the credit to 8% and expand the credit for agricultural purposes and mineral extractions. \$70 million.
- ◆ *(Extends the Sunset for the Manufactures' Investment Credit and Exemption).* Extends the sunset date from January 1, 2001 to January 1, 2008. Assembly and Senate Republicans support elimination of the sunset date.

- ◆ *(Increases Capital Gains Exclusion for Small Business Stock).* Increases the existing 50% exclusion for the sale of small business stock gains to 100%, at a cost of \$30 million in 2006-07. The stock must be held for more than five years and purchased after January 1, 2001.

PUBLIC SAFETY

In the public safety area the May Revision proposes a \$32.2 million net reduction in the Governor's Budget. This is a relatively small reduction given the state's worsening fiscal situation. Only three departments will actually receive a net reduction in funding in the Budget Year: the Office of Criminal Justice Planning, the Judiciary, and the Department of Corrections. Almost all of this reduction is simply the Department of Correction's annual adjustment for population workload, which reflects the need for reduced resources with a declining population. Overall, the proposed funding seems to be consistent with the recent Assembly Republican request that the Governor not cut public safety departments. While there are a fair amount of small program increases, the Governor has not included any significant new policy proposals.

- ◆ ***Additional DNA Laboratory Space (\$2.1 million GF)***– With the additional demand for DNA typing in court cases and criminal justice investigations, the Department of Justice is proposing to expand its laboratory facilities to the city of Richmond. The May Revision proposes \$2.1 million for lease and improvements of a new site, which will accommodate positions requested in the Governor's Budget. This facility would be separate from the new \$15 million DNA laboratory proposed in the Governor's Budget.
- ◆ ***Energy Investigation and Litigation (\$5.4 million GF)*** – The May Revision proposes an additional \$5 million to expand the existing \$4 million proposal for an Energy Task Force to investigate and prosecute cases of market manipulation by energy generators and natural gas suppliers.
- ◆ ***Fixing the Capitol (\$870,000 GF)*** – In an attempt to recover some portion of the \$16.5 million in damage caused to the State Capitol Building from the January automotive incident, the Governor proposes to increase the Department of Justice budget by \$870,000. This funding will be used to retain counsel and other specialized consultants that will negotiate or litigate potential payments from insurance companies to cover the cost of repairs.
- ◆ ***Cal-Photo Underdeveloped (-\$1.2 million GF)*** – The Administration proposes deletion of \$1,157,000 to expand the Cal-Photo Central Index to 10 law enforcement agencies in the Northern and Central California regions. This new system would allow local law enforcement agencies to exchange photographs and information over a computer network, thereby increasing access to investigative information.
- ◆ ***Corrections Population Drops Again (-\$81 million GF)*** – For the second year in a row the Department of Corrections has projected a decline in population. This decline of inmates in prison and on parole will result in a General Fund savings of approximate \$81 million.
- ◆ ***Administrative Segregation (\$12 million GF)*** – The Governor is proposing an augmentation of \$12 million to increase staffing for existing Administrative Segregation Units. This standard will ensure a necessary level of custodial supervision and clinical staffing.
- ◆ ***DNA Sampling for Inmates (\$1.8 million GF)*** – The May Revision includes \$1,753,000 for record searches, DNA collection and palm print identification for specified inmates. This will allow the department to comply with mandates involving post-conviction testing and expand current programs to input samples into the DOJ database.

- ◆ **Youth Authority Dumps Apple (\$1.1 million GF)** –The Youth Authority is requesting \$1.1 million to transfer their existing computer system to a Windows environment. Currently the department operates an Apple/ Macintosh series of computers, which according to the department are “ inconsistent with the overall government technology marketplace.”
- ◆ **Less Equipment for the War on Meth (-\$10 million GF)** –The Governor is proposing to reduce his January 10 proposal to expand the Central Valley HIDA by nearly \$40 million. The original plan included \$15 million for ongoing support and \$25 million for equipment grants. This cut would represent a \$10 million decrease in the equipment grant, leaving a total of \$30 million.
- ◆ **Law Enforcement Training Centers (\$5 million GF)** –This augmentation would provide funding for three regional training centers. These centers are located in Los Angeles, San Diego, and Sacramento.
- ◆ **Governor Denies Equal Access (-\$5 million GF)** –The Governor is proposing to eliminate the \$5 million augmentation to the Equal Access Fund. This fund provides legal services for an estimated 7.2 million persons in California who are unable to afford them. With this deletion the fund would still have \$10 million in the base.
- ◆ **Judicial Management Systems Funded (\$1.5 million)** –The May Revision includes \$1.5 million for the implementation of a standardized financial management system for the trial courts. This will allow the courts to comply with the Lockyer-Isenberg Trial Court Funding Act of 1997, which requires the courts to sever their business and computer services relationships with the counties.
- ◆ **Security Negotiated Salary Increases (\$4.8 million)** -- The May Revision proposes \$4.8 million to support negotiated salary agreements for court security personnel. Negotiated Salary Increases will allow the courts to continue existing security services and provide increased security where necessary